

Decision 02-08-073 August 22, 2002

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Joint Application of AT&T Communications of California, Inc. (U 5002 C) and WorldCom, Inc. for the Commission to Reexamine the Recurring Costs and Prices of Unbundled Switching in Its First Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 01-02-024
(Filed February 21, 2001)

Application of AT&T Communications of California, Inc. (U 5002 C) and WorldCom, Inc. for the Commission to Reexamine the Recurring Costs and Prices of Unbundled Loops in Its First Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 01-02-035
(Filed February 28, 2001)

Application of The Telephone Connection Local Services, LLC (U 5522 C) for the Commission to Reexamine the Recurring Costs and Prices of the DS-3 Entrance Facility Without Equipment in Its Second Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 02-02-031
(Filed February 28, 2002)

Application of AT&T Communications of California, Inc. (U 5002 C) and WorldCom, Inc. for the Commission to Reexamine the Recurring Costs and Prices of Unbundled Interoffice Transmission Facilities and Signaling Networks and Call-Related Databases in Its Second Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 02-02-032
(Filed February 28, 2002)

Application of Pacific Bell Telephone Company (U 1001 C) for the Commission to Reexamine the Costs and Prices of the Expanded Interconnection Service Cross-Connect Network Element in the Second Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 02-02-034
(Filed February 28, 2002)

Application of XO California, Inc. (U 5553 C) for the Commission to Reexamine the Recurring Costs of DS1 and DS3 Unbundled Network Element Loops in Its Second Annual Review of Unbundled Network Element Costs Pursuant to Ordering Paragraph 11 of D.99-11-050.

Application 02-03-002
(Filed March 1, 2002)

OPINION MODIFYING DECISION 99-11-050 TO REMOVE RESTRICTION ON REVIEW OF THE SHARED AND COMMON COST MARK-UP

I. Summary

This decision modifies Decision (D.) 99-11-050 to remove a restriction contained in that order regarding review of the shared and common cost

mark-up of 19%. This modification is made in response to a remand of the Commission's calculation of the total direct cost of providing unbundled network elements (UNEs) by the U.S. District Court for the Northern District of California. (*AT&T Communications of California Inc. et al., v. Pacific Bell Telephone Company, et al.* Order on Cross-Motions for Summary Judgment No. C01-02517 (CW) (N.D. Cal. August 6, 2002). The total direct cost of UNEs is a component of the mark-up calculation. The Court found that the Commission made a double-counting error when it calculated this number. The assigned Administrative Law Judge (ALJ) will issue a further ruling in this docket allowing parties to comment on how the Commission should correct the double-counting error found by the U.S. District Court.

II. Background

In D. 99-11-050,¹ the Commission adopted prices for the UNEs that Pacific Bell Telephone Company (Pacific) sells to competitors who use portions of its network. One component of the prices adopted in that order was a percentage mark-up over the forward-looking cost of UNEs to recover Pacific's "shared and common costs."² The Commission adopted a mark-up percentage of 19% based

¹ D.99-11-050 was issued in the Commission's Rulemaking and Investigation to Govern Open Access to Bottleneck Services and Establish a Framework for Network Architecture and Development of Dominant Carrier Networks (Rulemaking 93-04-003/ Investigation 93-04-002) ("OANAD proceeding").

² Shared and Common costs are defined in Appendix C of D.95-12-016. According to page 6 of Appendix C, shared costs are defined as "costs that are attributable to a group of outputs but not specific to any one within the group, which are avoidable only if all outputs within the group are not provided." Common costs are defined as "costs that are common to all outputs offered by the firm." The Federal Communications Commission has defined "forward-looking common costs" as "economic costs efficiently incurred in providing a group of elements or services (which may include all

Footnote continued on next page

on a calculation of Pacific's shared and common costs divided by the total direct costs of UNEs and total non-recurring costs adopted in D.98-12-079.

(D.99-11-050, mimeo. at 72, and 257.) Essentially, for each of the UNEs that Pacific sells to competitors, the UNE cost is increased by 19% to establish a UNE price.

At the same time the Commission adopted UNE prices in 1999, it noted the need to address the future status of the prices it was setting. Therefore, D.99-11-050 established a process for an annual reexamination of the costs of no more than two UNEs. (*Id.*, at 168-169.) The order specified, however, that the Commission would not entertain requests to reconsider the 19% markup for shared and common costs in any annual cost reexamination proceeding. (*Id.*, at 169, n. 155, and 272.) The Commission is currently reviewing the costs of several UNEs in the above-captioned proceeding (also referred to as the "2001/2002 UNE Reexamination").³

AT&T Communications of California, Inc., MCI Worldcom Network Services, Inc. and MCImetro Access Transmission Services LLC (jointly "Plaintiffs") filed a suit in U.S. District Court seeking to overturn aspects of D.99-11-050 related to the shared and common cost mark-up. Plaintiffs argued

elements or services provided by the incumbent [local exchange carrier]) that cannot be attributed directly to individual elements or services." (47 C.F.R. 51.505(c)(1).)

³ Indeed, in the 2001/2002 UNE Reexamination, AT&T Communications of California, Inc. and WorldCom, Inc. ("Joint Applicants") have made repeated requests for review of the 19% mark-up. In light of the language contained in D.99-11-050 restricting review of the mark-up, this request was first denied by the Assigned Commissioner and ALJ in a ruling of 6/14/01, and subsequently denied in rulings of 7/11/01 and 6/12/02.

that the Commission improperly determined Pacific's firm-wide shared and common costs and unreasonably allocated these costs only to UNEs. In a cross-motion, Pacific argued that the Commission's OANAD decisions contained other errors because they rejected Pacific's proposed risk adder, double-counted non-recurring costs, failed to set a recurring rate for OSS costs and erroneously ordered Pacific to provide CLCs with combination of UNEs at cost-based prices.

On August 6, 2002, the U.S. District Court issued its order in *AT&T v. Pacific Bell*. The court denied all of Plaintiff's claims and denied all but one of Pacific's claims. The court agreed with Pacific that the Commission had double-counted non-recurring costs when it calculated Pacific's total direct costs of UNEs. The order states, "The [Commission's] determination of Pacific's direct cost of providing UNEs (the denominator of the common cost mark-up), and any decision which relies on this determination, must be vacated and remanded, so that the double-counting can be remedied." (*AT&T v. Pacific Bell*, slip op. at 38.)

III. Discussion

Based on the remand contained in the order of the U.S. District Court in *AT&T v. Pacific Bell*, the Commission is obligated to review the shared and common cost mark-up adopted in D.99-11-050. The logical place for the Commission to undertake this review is within the currently open 2001/2002 UNE Reexamination, where we are already reviewing UNE prices. Therefore, we should modify the restriction the Commission initially placed on this review and allow it to proceed within the scope of the currently open 2001/2002 UNE Reexamination Proceeding.

The assigned ALJ should issue a subsequent ruling in this docket to initiate the adjustment directed by the Court's remand order. That ruling should allow parties an opportunity to comment on how the Commission should proceed and

what Commission orders might be impacted. The ruling should ask parties to comment on the correct methodology to be used to adjust the calculation of the total direct costs of UNEs. For example, should the Commission correct any double-counting by subtracting \$583 million from the denominator of the mark-up calculation adopted in D.99-11-050? The ruling should also ask for comment on whether any changes to the mark-up calculation should apply retroactively to the effective date of D.99-11-050 or prospectively only.

IV. Comments on Draft Decision

Pursuant to Rule 77.7(f) of the Commission's Rules of Practice and Procedure, the Commission may reduce or waive comments in an unforeseen emergency situation. Rule 81(g) states that a deadline for Commission action imposed by a court is an example of an unforeseen emergency. The remand order contained in *AT&T v. Pacific Bell* constitutes an unforeseen emergency because the court has placed a level of uncertainty over the UNE prices contained in D.99-11-050, D.02-05-042, and interconnection agreements between Pacific and competitive local carriers. Therefore, we will reduce the standard time frame for comments on this order so that the review of the remanded matter can be initiated as soon as possible. Parties shall have seven days to comment on this order. No reply comments will be permitted.

The Commission mailed the draft decision of the ALJ in this matter to the service list for the OANAD proceeding and the parties in the 2001/2002 UNE Reexamination. Comments were filed by Pacific and Joint Applicants.

Pacific comments that the Commission need not resolve the issues raised by the Court's remand order prior to evaluating Pacific's application under Section 271 to provide in-region long distance service. According to Pacific, the Commission can simply declare the current mark-up percentage of 19% interim

and subject to true-up while it corrects the mathematical error found by the court. Pacific believes this can be accomplished without reexamining any other aspects of shared and common costs. Therefore, Pacific suggests removing any language in the draft order that lifts the restriction in D.99-11-050 on review of the shared and common cost mark-up.

Joint Applicants do not agree that any double-counting has occurred in the mark-up calculation. Nevertheless, they suggest the Commission modify the draft order to require a recalculation of the shared and common cost mark-up based on current cost data. Joint Applicants maintain that the use of current cost data is preferable to any correction using what Joint Applicants characterize as an “egregiously out-of-date” record from the OANAD proceeding. They describe several purported pitfalls in attempting to correct the double-counting found by the Court using the original OANAD record. In addition, they claim that setting a shared and common cost mark-up based on the original OANAD record would violate forward-looking cost principles. Rather, Joint Applicants suggest an adjustment to the mark-up using current and publicly reported cost data.

We decline to make any changes to this order in response to the comments. Pacific’s request that we declare the 19% mark-up interim and subject to true-up should be addressed later, after we have received comments from parties on whether to handle any mark-up adjustments retroactively or prospectively. Further, we disagree with Pacific that it is unnecessary to remove the restriction in D.99-11-050 on review of the mark-up calculation. This modification is necessary to give the Commission the option of a thorough review of the mark-up calculation. Where Joint Applicants argue that there was no double-counting, these arguments are more appropriately the subject of any appeal to the Court’s

remand order. Finally, where Joint Applicants discuss how we should go about adjusting the shared and common cost mark-up in response to the remand order, the issues they raise are more appropriately addressed when we actually perform the review in the UNE Reexamination proceeding.

Findings of Fact

1. D.99-11-050 states that the Commission shall not consider any requests to change the 19% mark-up for shared and common costs within the scope of the annual UNE cost reexamination proceeding.

2. On August 6, 2002, the U.S. District Court issued an order in *AT&T v. Pacific Bell* that remanded to the Commission its calculation of the shared and common cost mark-up contained in D.99-11-050, and any decision that relies on this calculation, to correct the double-counting of non-recurring costs.

Conclusions of Law

1. In light of the remand order of the U.S. District Court, Ordering Paragraph 12 of D.99-11-050 should be modified to remove the restriction on consideration of the shared and common cost mark-up within the annual cost reexamination proceeding.

2. To comply with the court's remand order, review of the calculation of Pacific's direct costs of UNEs, and adjustments to all relevant decisions that depend on this calculation, should occur within the scope of the 2001/2002 UNE Reexamination proceeding.

3. The U.S. District Court remand order constitutes an unforeseen emergency.

O R D E R

IT IS ORDERED that:

1. Decision 99-11-050 is modified to remove Ordering Paragraph 12 and footnote 155 on page 169.
2. The Commission shall review the calculation of Pacific Bell Telephone Company's direct costs of unbundled network elements (UNEs) within the scope of the 2001/2002 UNE Reexamination proceeding. The assigned Administrative Law Judge shall issue a ruling allowing parties an opportunity to comment on how the Commission should correct the double-counting error found by the U.S. District Court.
3. This decision should be mailed to the service list for Rulemaking 93-04-003/Investigation 93-04-002 (OANAD proceeding).

This order is effective today.

Dated August 22, 2002, at San Francisco, California.

LORETTA M. LYNCH
President
HENRY M. DUQUE
CARL W. WOOD
GEOFFREY F. BROWN
MICHAEL R. PEEVEY
Commissioners